

INITIAL STATEMENT OF REASONS

Community Development Block Grant (CDBG) Title 25, California Code of Regulations

Proposed Amendments to Sections 7056, 7060, 7062.1, 7064, 7066, 7078.4

INTRODUCTION

This Initial Statement of Reasons (ISOR) has been prepared by the California Department of Housing and Community Development (hereinafter “the Department”) to describe amendments to regulations currently in effect for the State Community Development Block Grant (CDBG) Program and the factual basis for these amendments.

The State of California receives money from the U.S. Department of Housing and Urban Development (hereinafter “HUD”) to make grants to units of general local government, which are too small to receive an entitlement amount directly from HUD. These funds can be used for a wide variety of eligible activities, including housing rehabilitation, housing new construction, housing acquisition, public works, community facilities, public services and economic development as long as the recipients comply with a comprehensive set of requirements prescribed by federal law and these State regulations.

CDBG funds are made available to cities and counties through Notices of Funding Availability (NOFAs), and applications are reviewed and evaluated using various criteria set forth in the State’s CDBG regulations.

In summary, the Department proposes to make the following changes:

- Require applicants to have resolved any performance problems for program income prior to being eligible to apply for State CDBG Program funds.
- Require grantees to submit program guidelines to the Department for review and approval before expending program activity funds. [This will ensure that the grantee’s guidelines address all the necessary state and federal regulations as listed in a typical standard agreement. The changed regulations also list out non-regulatory requirements which cover standard lending and construction practices and ensure that the program guidelines award the funds in a non-arbitrary and consistent manner. State staff believes these additional requirements will assist grantees in having higher quality programs with fewer public complaints.](#)
- If an applicant has been funded for multiple annual award amount under the multiple year award and any year is less than the \$500,000 annual cap, then the grantee can apply for additional funds up to the cap amount for that year.

- Change the date for removing the funding cap for Economic Development Over-the-Counter projects from December 31st to September 1st.
- Allow applicants to apply for multi-year awards, up through three funding cycles, with a maximum annual award of \$500,000 and of \$1,500,000 for three years.
- Remove the phasing requirement for multiple funding year applications.

DISCUSSION OF PROPOSED AMENDMENTS

Summary of Amendments to Section 7056:

Existing general program regulations do not address an applicant's performance as it pertains to program income. The expenditure and reporting of program income is important because it relates to requirements for grant activities under the federal CDBG regulations, 24 CFR 570.489(e)(3)(ii). Section 7056 is being amended to include performance problems for program income as a matter that has to be resolved prior to submittal of an application. In addition, Section 7056 is being amended to add disencumbrance as an additional action that can resolve a performance problem. It is proposed that Grantees be specifically offered disencumbrance of funds as a way to resolve performance problems prior to draw down of grant funds. A case in which a grantee has missed its expenditure milestones would be a use for this action, because un-drawn funds related to the missed milestones could be disencumbered to resolve the performance problem. It will allow the Department to reassign the unused funds to good performers and ensure the CDBG funds are expended quickly in order to comply with HUD's expenditure requirements

This Section is also being revised to reduce the term of standard single year grant awards from 30 months to 24 months and to clarify the standard contract periods for multi-year grant awards (up to three years of funding). The contract time reduction period is needed because the state of California is one of the poorest performers, in terms of expending funds promptly. Staff learned that California is the only State which allows grantees 30 months to expend their funds. Most other states have much shorter contract periods. The 24 month time period is the longest which other states provide.

Lastly, this section is being revised to require grantees to submit their program guidelines into state staff for review and approval. In the past the practice of the program was to review program guidelines as part of the rating and ranking process. By using the rating and ranking system to review the proposed program guidelines, the program guidelines for program income funded programs do not get reviewed. Rather than submit program income program guidelines with an application that may have nothing to do with that activity, the program has determined that submitting the program guidelines for approval prior to drawdown of funds is more appropriate. In addition, this review requirement is needed to ensure that grantee's program guidelines are complying with HUD federal regulations and with State regulations. Further non-regulatory requirements have been listed to ensure reasonable lending practices and non-arbitrary award of funds. This list of requirements will also assist the grantee in producing guidelines which ensure quality projects and minimize public complaints.

7056. Application and Funding Requirements.

(a) The applicant shall meet the following requirements when the application is submitted:

(1) The applicant shall submit all the application information required in Section 7026.1 and/or Section 7070 as applicable.

(2) The applicant shall have resolved any audit findings, performance problems for program income or performance problems for prior CDBG grants awarded by an urban county, by HUD under the Small Cities Program or by the State under this subchapter. The Director may waive this requirement when such problems or findings result in no obligation to return funds to the grantor, arrangements satisfactory to the grantor have been made for repayment, disencumbrance, ~~or~~ performance, or a formal action to resolve the matter has been taken.

(b) Applicants shall meet the following requirements prior to an award of grant funds:

(1) As a condition of receiving funds pursuant to this subchapter, an eligible city or county shall have submitted a housing element to the Department in accordance with the requirements of Article 10.6 (commencing with Section 65580) of Chapter 3 of Division 1 of Title 7 of the Government Code. However, except as otherwise provided in Section 50830 of the Health and Safety Code, no application for funds shall be denied because of the content of the housing element or because of the findings made by the Department pursuant to Section 65585 of the Government Code.

(2) (A) Except as otherwise provided in subparagraphs (B) and (C), no city or county shall be eligible to receive funds pursuant to this Subchapter if the city or county has adopted a general plan, ordinance, or other measure which directly limits, by number, either of the following:

1. The building permits that may be issued for residential construction.
2. The buildable lots which may be developed for residential purposes.

(B) Subparagraph (A) shall not apply to either of the following:

1. An ordinance adopted by a city or county which does any of the following:
 - a. Imposes a moratorium, to protect the public health and safety, on residential construction for a specified period of time, if, under the terms of the ordinance, the moratorium will cease when the public health or safety is no longer jeopardized by the construction.
 - b. Creates agricultural preserves pursuant to Chapter 7 (commencing with Section 51200) of Part 2 of Division 1 of Title 5 of the Government Code.
 - c. Was adopted pursuant to a specific requirement of a state or multi-state board, agency, department, or commission.
2. A city or county which has a housing element that the department has found to be adequate pursuant to subdivision (c) of Section 65585 of the Government Code or which is deemed to be in compliance with the requirements of Article 10.6 (commencing with Section 65580) of Chapter 3 of Division 1 of Title 7 of the Government Code pursuant to Section 65586 of the Government Code at the time the city or county applies for funds under the program, unless a final order has been issued by a court in which the court determined that the housing element is not in compliance with Article 10.6 (commencing with Section 65580) of Chapter 3 of Division 1 of Title 7 of the Government Code.

(C) A city or county which has adopted a general plan, ordinance, or other measure subject to the restrictions of subparagraph (A), which are not exempted by subdivision (B), may, notwithstanding subparagraph (A), receive funds pursuant to this subchapter if the use of the funds is restricted for housing for the targeted income group. However, applications from cities or counties which have not adopted a general plan, ordinance, or other measure subject to the restrictions of subparagraph (A) shall, to the extent that eligible applications for grants exceed the amount available for distribution pursuant to this Subchapter have priority over applications from cities or counties which have adopted such a general plan, ordinance, or other measure which are not exempted by subdivision (B).

(3) At least fifty-one percent (51%) of the funds applied for shall benefit the targeted income group. No activity or portion of a program assisted by these funds may exclude from its benefits the lowest targeted income group. Individual activities shall meet one of the three national objectives which are: (1) the development of viable urban communities by providing decent housing and a suitable living environment and expanding economic opportunities, principally for persons of low- and moderate-income (TIG); (2) aiding in the prevention or elimination of slums or blight; or (3) meeting other community development needs having a particular urgency. For the purposes of this section, "slums" and "blight" means a blighted area or structure characterized by one or more of the following conditions: (1) the buildings and structures, used or intended to be used for living, commercial, industrial, or other purposes, which are unfit to occupy for such purposes and are conducive to ill health, transmission of disease, infant mortality, juvenile delinquency, and crime because of factors listed in [Health and Safety Code Section 33031](#); and (2) properties which suffer from economic dislocation, deterioration, or disuse because of factors listed in [Health and Safety Code, Section 33032](#). For the purposes of this section, an activity will be considered to address the standard of urgency if the applicant certifies that the activity is designed to alleviate existing conditions which pose a serious and immediate threat to the health or welfare of the community which are of recent origin or which recently became urgent, that the applicant is unable to finance the activity on its own, and that other sources of funding are not available to meet such needs. For the purposes of this section, any condition which has existed longer than eighteen (18) months prior to the final filing date for applications shall not be considered to meet the standard of urgency.

(4) The single-year program described in the application must be scheduled for completion within ~~thirty (30)~~ twenty four (24) months from the date the grant agreement is executed by the State. The multi-year, two or three year program described in the application must be scheduled for completion within 36 or 48 months, respectively. The Department may waive this provision in writing if it determines that the program, by its nature, cannot be completed within ~~thirty (30) months~~ the 24, 36, or 48 month period, or that conditions beyond the grantee's or State's control hinder program completion.

(5)(A) If CDBG grant funds or local program income will be used to operate a program (i.e., activities serving multiple separate projects, not persons), the applicant shall submit program guidelines to the Department for approval. No CDBG grant funds or

local program income shall be expended to operate a program until the Department has approved the program guidelines in writing.

(B) The program guidelines shall describe how the program will be operated and how it will comply with State and federal regulations. In addition, program guidelines shall address the following topics:

- i. Loan terms and interest rates;
- ii. Loan underwriting standards;
- iii. Loan application processing procedures and timing for loan approvals;
- iv. Procedures for resolving disputes between the participant and the CDBG grantee;
- v. Description of any property restrictions imposed as a condition of receiving the loan (e.g., resale controls, equity sharing);
- vi. Loan servicing policies addressing the issues of: subordination; refinancing; change in occupancy, change in use, assumptions, and verification of payment of taxes and insurance.
- vii. If the program will involve rehabilitation or construction, procedures for developing the scope of work, description of the contractor procurement and payment process, and a description of the conflict resolution process in the event of a dispute between the contractor and the program participant.

Note: Authority cited: [Sections 50406\(h\) and \(n\), Health and Safety Code](#); and [24 CFR 570.489\(b\)](#). Reference: [Sections 51200, et seq., and Sections 65580 et seq., Government Code](#); [Sections 33031, 33032, 50406, 50407, 50829 and 50830, Health and Safety Code](#); [42 U.S.C. 5304 and 5306](#); [24 CFR 570.489\(a\) and \(b\)](#) and [24 CFR 570.901\(b\)\(3\)](#).

Summary of Amendments to Section 7060

Existing regulations permit eligible applicants to submit one application per year under either the general allocation or economic development allocation not to exceed \$500,000. If the applicant applies for both allocations then the total annual funding is limited to \$800,000. Under the recommended change in Section 7064, an applicant can apply for general allocation funds for up to three annual funding awards. This change is proposed to increase the expenditure rate of grantees. By having projects approved for the next two or three funding cycles, grantees will be better able to plan for and implement future funding. If the applicant is awarded funds for all three years and the award per year is less than the \$500,000 annual cap noted in Section 7060, then that applicant is allowed to apply for the difference between the amount of funds they have secured annually under the multi-year funding award and the \$500,000 annual cap. This change is proposed to allow applicants to access the full amount of grant funds available under Section 7060 while having a multi-year funding award in place.

7060. Eligible Applicants.

Any city or county is eligible to apply for the State CDBG Program except a city or county which participates in or is eligible to participate in the HUD administered Community Development Block Grant Entitlement Program. The following restrictions shall apply to all applicants under the State Program.

(a) Except as provided in the Sections 7062 and 7062.1, an applicant may submit only one application each funding cycle for activities in its jurisdiction. A grantee receiving a grant award for ~~two~~ up to three consecutive annual funding awards cycles pursuant to Section 7064(c) that does not undertake the portion of the program funded from the second or third funding cycle may submit a new application provided the multi year award ~~first year program~~ has been terminated under the terms of the grant agreement. A grantee that has received a ~~grant~~ multiple year award for ~~two~~ up to three years consecutive funding cycle, where any of the annual awards is less than \$500,000, may submit an application under the second and/or third year funding cycle for ~~second~~ additional awards, which when combined with their existing annual funding awards, do not to exceed \$1 million less the amount of the first award \$500,000 per year.

Summary of Amendments to Section 7062.1 .

This change is under 7062.1(a)(6) and will move the funding cap waiving date, from December 1 to September 1, for Economic Development Funding applications. This change will make the State Regulation the same as Statute Section 50832(a). The change is necessary because the state program is now receiving a large number of funding requests for larger infrastructure projects which require the larger amounts of funds provided after the waiver date. By moving the waiver date to earlier in the year, the state EDBG program will be able to award funds earlier to grantees with infrastructure requests and they in turn will be able to spend those funds more quickly. By spending the funds more quickly, state staff will improve the expenditure rate and move closer to meeting the expenditure requirements which HUD has set for state grantees. If approved, this change will facilitate the funding of larger ED infrastructure projects earlier in the funding year and allow for funds to be expended earlier such that HUD expenditure milestones can be met.

7062.1. Special Allocation for Economic Development.

(a) (6) Funding maximums from the Economic Development Allocation and the Planning component shall be set forth in Health and Safety Code Section 50832 subdivision (a) and Section 50833 subdivision (a) and (b). The Department may waive the eight hundred thousand dollar (\$800,000) and five hundred thousand dollar (\$500,000) limitation for the Economic Development Allocation after ~~December 31~~ September 1 of each year.

(d) Planning and Technical Assistance Component. Through the Planning and Technical Assistance Component ("Planning Component"), eligible cities and counties may apply for, and the department may award, grants for economic development planning and technical assistance activities. No single city or county shall receive more than two grants or thirty five thousand dollars (\$35,000) per year. Two or more applicants which share a planning program may submit a joint application. The

maximum award for a joint application shall be thirty five thousand dollars (\$35,000) per participating applicant.

Summary of Amendments to Section 7064

Section 7064 is being amended to allow applicants to secure funds for activities over a period of three annual funding awards instead of just two. The maximum grant award is being raised to \$1,500,000 to correspond with the maximum annual award limit of \$500,000 per year for the multi- year award. . This will be consistent with [Statute Section 50832\(a\)](#). This awarding of future funds will reduce the administrative burden for applicants and the Department. There will be fewer applications, contracts and reporting. It will provide a seamless funding stream for on going housing rehab and home buyer programs.

The third change to this Section is to take out the language which, for multi-year funding awards, requires the applicants to document that the proposed project or program cannot be phased over a period of several single year funding awards. This will allow for a larger number of multi-year funding awards for programs and projects and be consistent with the other changes in these regulations regarding multi-year funding awards. The CDBG program has identified two problems that this change will address. One, grantees are slow to expend funds in the first 12 months of their contracts and two; they have an administrative burden with administering grants. By awarding funding for up to 3 years, the grantees will be able to better forecast their funding streams for their projects and programs. This stability should increase their expenditure rates as well as provide administrative relief. By awarding the funds at once and generating one contract the grantees will not have to apply in the following two funding cycles and will not need new contracts and will not have to prepare reports for each contract. This will provide administrative relief not only to the grantees but to the Department.

7064. Grant Funding.

- (a) The amount of funds available for grants is equal to the total allocation of federal funds made available to the State under the Act after subtracting an allowable amount for State administrative costs. Grant funding is subject to the availability of federal funds.
- (b) Eligible applicants may apply for funds to undertake any one or any combination of the eligible activities described in Section 7058.
- (c) Except as provided in Section 7062.1, applicants may apply for funds ~~in~~ [from](#) either one, ~~or two~~ [or three annual](#) consecutive funding [awards](#) ~~cycles~~. The maximum grant amount per application for one funding award ~~cycle~~, regardless of the number of cities and counties included in the application, is five hundred thousand dollars (\$500,000). The maximum grant amount per application for ~~two~~ [up to three annual](#) consecutive funding [awards](#) ~~cycles~~ regardless of the number of cities and counties included in the

application, is one million, five hundred thousand dollars (\$1,000,000 1,500,000). Funds applied for under Section 7062 are not included in these funding maximums. There is no maximum amount for applications submitted under Section 7062 other than the amount of funds set aside for this purpose. ~~Applications for a grant for two consecutive funding cycles will only be funded by the Department when the applicant is applying for a single activity which cannot be completed in segments.~~ In the annual application process, priority for funding will be given to applicants that received prior State approval for a grant for ~~at the~~ second or third year funding award ~~cycle~~. These priorities are subject to the availability of federal funds and the satisfactory performance by grantees. If federal funding to the State is insufficient to meet commitments for the second or third part of a two or three year funding ~~cycle~~ award, the Department will establish a procedure for awarding available funds based on previous rankings and program performance.

Note: Authority cited: [Sections 50406\(h\) and \(n\), Health and Safety Code](#). Reference: [Section 50832\(a\), Health and Safety Code](#); and 42 U.S.C. 5306(d)(2).

Summary of Amendments to Section 7066

Section 7066 is being amended to be consistent with Section 7064, which allows for multi-year funding of programs and projects, and to clarify how disencumbrances can be used to maintain eligibility for funding. Currently there is no method to address the situation that arises when a grantee is not expending funds on a timely basis and the grantee disencumbers some of the grant in order to achieve a milestone. It will allow for the Department to reassign the unused funds to good performers and ensure the CDBG funds are expended quickly in order to comply with HUD's expenditure requirements

7066. Procedure for Continuation of Funding.

(a) Grantees with prior State approval for two or three year funding ~~cycle~~ awards shall notify the Department in writing by the final date for submitting applications of their intent to continue the second or third year part of their program. Failure by the Grantee to so notify the Department will be deemed a waiver of continued funding.

(b) Funding will be continued provided adequate funds have been received by the Department from HUD, and the Grantee has performed in accordance with the grant agreement. Disencumbrance of funds not expended in accordance with the grant agreement and the performance measures described in Sections 7078.4 and 7062.1(b)(7) shall constitute satisfactory performance under the grant agreement.

Note: Authority cited: [Sections 50406\(h\) and \(n\), Health and Safety Code](#); 24 CFR 570.489(b). Reference: [Sections 50406 and 50407, Health and Safety Code](#); 42 U.S.C. 5306(d)(2) and (3); 24 CFR 570.489 and 570.491.

Summary of Amendments to Section 7078.4

Section 7081.4 is being amended to bring the program milestones for each of the eligible activities in line with the new reduced State CDBG Program contract period for single year awards of twenty four (24) months, per revision of Section 7056. The Milestones for the single year awards will be used as part of performance under the rating and ranking process. This section is also being amended to include language about milestones for multi-year awarded activities and disencumbrance of funds for poor performers. This disencumbrance of funds is needed to ensure that grantees who are not performing on their multi year awards do not hold up CDBG funds which could be used by other eligible applicants for their programs or projects. It will allow for the Department to reassign the unused funds to good performers and ensure the CDBG funds are expended quickly in order to comply with HUD's expenditure requirements.

7078.4. Prior Performance Operating CDBG Grants (150 points).

(c) The Department shall rate applicant's performance based on the following criteria:

~~(1) For housing rehabilitation activities, competitive applicants will have expended 25 percent of awarded dollars by the twelfth month of the State CDBG contract, and 75 percent by the twenty fourth month.~~

(1) For housing rehabilitation program, housing acquisition program, public works, housing new construction, community facilities, and public service activities under a single year funding award 24 month contract, competitive applicants will have expended twenty five (25%) of awarded dollars by the twelfth month of the State CDBG Program contract and seventy-five percent (75%) by the eighteenth (18th) month. Grantees that do not make the 25% milestone will receive a hold out letter for the next funding cycle. A waiver from hold out status may be granted if the grantee makes the 75% milestone by the 18th month. Grantees may choose to disencumber the difference in funds between what they have expended and the amount of the 75% milestone and so come into compliance with CDBG performance milestones and obtain a waiver.

~~(2) For public works, community facilities, and new construction activities, competitive applicants will have expended 50 percent of awarded dollars by the eighteenth month and 75 percent by the twenty fourth month.~~

~~(3) For public services, competitive applicants will have expended their CDBG dollars on a timely basis throughout the grant term while the service is being provided.~~

(2) For each program activity with multi-year funding awards, grantees will have milestones for each year of funding. If Grantees do not spend twenty-five percent (25%) of their first year of funding by the twelfth month, then the Department will disencumber the difference between what was expended for that program activity and

the 25% milestone. In the same way, if grantees do not spend seventy-five percent (75%) of their annual award at the 18th month, then the Department may disencumber the difference between what was expended for the program activity and the 75% milestone. Any unexpended funds for that specific activity under the specific annual award will be disencumbered after the 24th month. This annual set of milestones will apply to each year of the multi year funding awards. This disencumberance of funds will not allow the grantee to apply for any additional funding in future application cycles other than the original difference, if any, as described in Section 7060 between annual award and maximum annual allowed (\$500,000). Having more than 50% of the multi year funding award disencumbered during the life of the program will be grounds for negative performance under rating and ranking.

(3) Grantees who have multiple year funding awards for single project specific activities, will designate in their application at what time the CDBG funding will be needed. Department staff shall assign milestones based on the project's timeline shown in the application if it does not hinder the Department's timely expenditure of CDBG funds. If the grantee does not meet the milestones assigned to the specific project, then Department staff may disencumber funds up to the designated milestone